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State of Idaho

Legislative Services Office

Management Report

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A communication to the Joint Finance-Appropriations Committee

# **IDAHO STATE LIQUOR DISPENSARY**

## **FY 2005, 2006, and 2007**

**Report IC18507**

**Date Issued: December 17, 2007**

*Serving Idaho's Citizen Legislature*

# FOREWORD

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## **PURPOSE OF REPORT**

We evaluated the internal controls over financial operations of the Idaho State Liquor Dispensary as part of our effort to evaluate each State agency at least once every three years. This report summarizes the results of our evaluation.

## **SCOPE OF WORK**

The management of the Dispensary is responsible for establishing and maintaining internal controls. We obtained an understanding of the relevant policies and procedures comprising the internal control system. We also determined whether the relevant policies and procedures had actually been placed into operation. Our intent was to indicate where internal controls could be improved in order to help ensure the Dispensary's ability to record, process, summarize, and report financial data accurately.

## **AUDIT AUTHORIZATION**

Reported to the Joint Finance-Appropriations Committee as directed by the Legislative Council of the Idaho Legislature, authorized by Idaho Code, Section 67-429.

## **ASSIGNED STAFF**

Kathleen Watkins, CPA, Auditor-in-Charge  
Maresa Blessinger, Staff Auditor

## **ADMINISTRATION AND TECHNICAL REVIEW**

Don H. Berg, CGFM, Manager, Legislative Audits Division  
April Renfro, CPA, Managing Auditor

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## EXECUTIVE SUMMARY LEGISLATIVE AUDITS

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### IDAHO STATE LIQUOR DISPENSARY

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**PURPOSE AND SCOPE** – We performed certain audit procedures to evaluate the effectiveness of the Idaho State Liquor Dispensary's internal control design and operation. The limited scope of our procedures does not allow us to give an opinion on the Dispensary's internal control system. Accordingly, we do not express an opinion or ensure that all instances of internal control weaknesses were disclosed. Our purpose was to indicate where internal controls could be strengthened to help ensure accurate financial statements and data. Any findings and recommendations are intended to improve the internal control system to prevent errors, omissions, misrepresentations, or fraud.

**CONCLUSION** – Although we include two findings and recommendations in this report, we conclude that the financial operations of the Dispensary meet accepted standards, and that the Dispensary substantially complies with laws, regulations, rules, grants, and contracts for which we tested compliance.

#### FINDINGS AND RECOMMENDATIONS

**FINDING #1** – Access to the computerized accounting system is inappropriately assigned. The Dispensary installed a new computerized accounting system in fiscal year 2005, and assigned significant access to several staff members to facilitate the installation process. Now that the system is fully installed and operational, some of these assignments are unnecessary or inappropriate and raise serious control issues. The current situation could allow changes to system processes or recorded transactions to occur, and such events would be difficult or impossible to detect.

For example, we noted that some staff members can initiate and also approve payments, or create and approve general ledger batches. In addition, several staff members have the ability to adjust inventory levels and pricing within the system, even though they are not directly responsible for maintaining the inventory records.

These situations indicate a significant lack of segregation of duties and further raise the risks that errors could occur and go undetected. Now that the system is fully functional, the assignment of rights and access should be reviewed and adjusted to establish appropriate controls and reduce these risks.

**RECOMMENDATION #1** – We recommend that the Dispensary evaluate each staff member's assigned rights and access to the computerized accounting system to ensure that job functions and activities are appropriately segregated. We also recommend that these assignments be periodically reviewed to identify changes as necessary.

**CORRECTIVE ACTION PLAN** – Our IT Department reviewed our ACCPAC accounting system access security tables, and has already removed non-essential users and administrative super-users from the system. Administrative rights are now restricted to appropriate IT personnel only. In addition, IT is currently reviewing the security tables with each department manager in order to evaluate each of their staff member's access to ensure it is commensurate with their assigned job responsibilities and that duties are appropriately segregated. This will be completed in January 2008.

**FINDING #2 – Time sheets are not properly signed or approved.** The Dispensary does not use the State's online time sheet entry system (I-Time) at all of its locations. The payroll clerk enters the information for employees at these locations, but some of these time sheets are not signed by the employee or approved by the supervisor. These signatures and approvals are significant controls that ensure reported time is properly submitted and accurate.

**RECOMMENDATION #2 – We recommend that** the Dispensary require that all time sheets have both the employee and supervisor signatures.

**CORRECTIVE ACTION PLAN** – We have recently installed DSL high speed internet access at the majority of our locations throughout the State. By the end of this fiscal year, we will have all but a few remote locations set up on the State's online time sheet entry system (I-Time), which will eliminate the potential for the vast majority of unsigned time sheets.

In the interim, our HR Department has already implemented the following procedures to ensure that all time sheets are signed by both the employee and supervisor.

- Time sheets are promptly submitted from each state liquor store for timely entry to I-Time by our payroll specialist. Time sheets submitted without proper signature require the employee's signature before the current SCO payroll processing cycle deadline. Supervisors will obtain the applicable employee's signature the next working day and forward that document by fax to the Payroll Department. The signed document will be stapled to the original faxed time sheet and the original will be kept on file at the store. These time sheets are marked "signature on file."
- Our Payroll Specialist has started an onsite training process with the State liquor stores on the use of I-Time. This program enables the personal password used by each employee to act as their signature. This training process is scheduled for completion by fiscal year end.

**PRIOR FINDINGS AND RECOMMENDATIONS** – The prior report had four findings and recommendations. As discussed below, all four findings are considered closed.

**PRIOR FINDING #1 – The Dispensary sells some products that it may not have legislative authority to sell.** Idaho Code, Section 23-203 authorizes the State Liquor Dispensary to regulate and sell alcoholic liquor. Alcoholic liquor is defined as any liquid or solid containing alcohol, spirits, wine, and any liquid or solid containing more than 4% of alcohol by weight. During fiscal year 2004, the Dispensary sold non-alcoholic items such as non-alcoholic mixers, cocktail recipe books, bar tools, ice, and cocktail garnishes. Although the revenue from the sale of these items is small when compared with total sales, the availability and sale of these products may be in violation of the Dispensary's authority. The sale of non-liquor items also adds to the administrative effort and cost to order, display, and account for these items.

**We recommended** that the Dispensary request an opinion from the Idaho Attorney General's Office to determine whether it has the authority to sell non-alcoholic items in the State-run stores.

**CURRENT STATUS: CLOSED** – This audit issue was corrected with the change to Idaho Code, Section 23-303 (c) which allows the liquor dispensary to sell non-alcohol merchandise related to the sale of alcoholic liquor.

**PRIOR FINDING #2.** The 2% surcharge required by Idaho Code is not assessed on some items, resulting in the Dispensary not collecting \$11,300. Idaho Code, Section 23-217 directs the Dispensary to include a 2% surcharge on the price of goods sold through its retail outlets. The surcharge is collected by the Dispensary and then remitted to the Drug and Family Court Services Fund. The pricing model used in formulating the retail price of goods sold, exempts all non-alcoholic items from the surcharge. During fiscal year 2004, non-alcoholic sales totaled approximately \$565,000, resulting in \$11,300 in related surcharges not being collected.

**We recommended** that the Dispensary apply the surcharge to all appropriate items sold, as directed by Idaho Code.

**CURRENT STATUS: CLOSED** – The Dispensary has applied the 2% surcharge to all items, including non-alcoholic items, effective February 1, 2005. In addition, the Dispensary's fiscal year 2006 appropriation required that it transfer the \$11,300 uncollected surcharge to the Drug Court and Family Court Services Fund on July 1, 2005.

**PRIOR FINDING #3.** The Dispensary does not have a procedure to determine changes in local option sales tax rates, resulting in \$25,000 that was not collected. Idaho Code, Section 63-2602 allows counties to elect to collect a local option tax. The tax is to be applied to all sales that are taxable under the State's sales tax regulations. Kootenai County held a special election in November 2003 and approved a 0.5% local option tax, effective April 1, 2004. The Dispensary did not adjust its operations to begin collecting the additional tax by the effective date. Collections of the local option tax did not begin until September 1, 2004. Based on county sales information, we estimate that the delay resulted in the loss of approximately \$25,000 in local option tax revenue for Kootenai County.

**We recommended** that the Dispensary implement procedures to ensure changes in the tax assessments are completed on the appropriate effective date.

**CURRENT STATUS: CLOSED** – The Dispensary's point of sale (POS) cash register system was not programmed or capable of charging any form of sales tax. The POS system has been reprogrammed to allow for sales tax collections, as well as to make changes to the tax rates at the beginning of any month. In addition, the Dispensary will request that the State Tax Commission notify the Dispensary whenever there is a change in any local county option sales tax.

**FINDING #4.** Sales tax is collected from the sale of non-alcoholic items, but not deposited in the Sales Tax Account. Idaho Code, Section 63-3638A states that sales tax collected on the sale of liquor is to be credited to the Liquor Fund rather than the Sales Tax Account. The Dispensary sells products that do not meet the definition of liquor. The Dispensary's pricing formula includes sales tax in the price applied to liquor and non-liquor products alike. During fiscal year 2004, the sale of non-liquor products generated approximately \$34,000 in sales tax revenue.

**We recommended** that the sales tax collected on the sale of non-liquor items be remitted to the appropriate account, as required by Idaho Code.

**CURRENT STATUS: CLOSED** – This audit issue was corrected with the change to Idaho Code, Section 63-3638 (a) which allows the sales tax of non-liquor merchandise to be deposited in the liquor fund.

**AGENCY RESPONSE** – Dispensary management has reviewed this report and its response is included in this report.

**FINANCIAL SUMMARY** – The following financial data is presented for informational purposes only.

**IDAHO STATE LIQUOR DISPENSARY – FY 2007 FINANCIAL SUMMARY**

|                        | Family<br>Court Services<br>Fund 0340 | Liquor Control<br>Fund 0418 | Total                |
|------------------------|---------------------------------------|-----------------------------|----------------------|
| Beginning Cash Balance | \$0                                   | \$12,112,742                | \$12,112,742         |
| Receipts               | 2,313,868                             | 119,669,016                 | 121,982,884          |
| Transfers-In           | 0                                     | 2,000,000                   | 2,000,000            |
| Total Cash Available   | <u>\$2,313,868</u>                    | <u>\$133,781,758</u>        | <u>\$136,095,626</u> |
| Personnel Costs        | \$0                                   | \$8,251,125                 | \$8,251,125          |
| Operating Expenditures | 0                                     | 69,907,818                  | 69,907,818           |
| Capital Outlay         | 0                                     | 1,258,633                   | 1,258,633            |
| Trustee and Benefit    | 2,313,868                             | 24,606,600                  | 26,920,468           |
| Transfers-Out          | <u>0</u>                              | <u>15,592,166</u>           | <u>15,592,166</u>    |
| Total Disbursements    | <u>\$2,313,868</u>                    | <u>\$119,616,342</u>        | <u>\$121,930,210</u> |
| Ending Fund Balance    | <u>\$0</u>                            | <u>\$14,165,416</u>         | <u>\$14,165,416</u>  |

**OTHER ISSUES.** Legislative auditors discussed other matters with the Dispensary's management which, if addressed, would improve internal control, compliance, and efficiency.

This report is intended solely for the information and use of the Idaho Liquor Dispensary and the Idaho Legislature and is not intended to be used by anyone other than these specified parties.

We appreciate the cooperation and assistance given to us by the superintendent, Dyke Nally, and his staff.

QUESTIONS CONCERNING THIS DOCUMENT SHOULD BE DIRECTED TO:

Don H. Berg, CGFM, Manager, Legislative Audits Division

April Renfro, CPA, Managing Auditor

# AGENCY RESPONSE

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C.L. "BUTCH" OTTER  
GOVERNOR

**STATE OF IDAHO**  
**LIQUOR DISPENSARY**  
*Executive Office of the Governor*

DYKENALLY  
SUPERINTENDENT

November 14, 2007

Don H. Berg  
Manager, Legislative Audits Division  
Legislative Services Office  
P. O. Box 83720  
Boise, ID 83720-0054

Dear Don:

It has again been our pleasure to work with your professional audit staff. We always appreciate your constructive comments and recommendations to improve internal controls at the Dispensary.

Following are our responses to the two findings included in your audit report for FY 2005, 2006, and 2007:

FINDING # 1 - Accounting System Access:

Our IT Department reviewed our ACCPAC accounting system access security tables, and has already removed non-essential users and administrative super-users from the system. Administrative rights are now restricted to appropriate IT personnel only. In addition, IT is currently reviewing the security tables with each department manager in order to evaluate each of their staff member's access to ensure it is commensurate with their assigned job responsibilities and that duties are appropriately segregated. This will be completed in January, 2008.

We will also review the security tables on an annual basis as part of the State of Idaho Management Control System internal controls review to identify any changes in staff responsibilities and system access as necessary.

FINDING # 2 – Time Sheets:

We have recently installed DSL high speed internet access at the majority of our locations throughout the state. By the end of this fiscal year we will have all but a few remote locations set up on the State's online time sheet entry system (I-Time), which will eliminate the potential for the vast majority of unsigned timesheets.

Don H. Berg  
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In the interim, our HR Department has already implemented the following procedures to ensure that all timesheets are signed by both the employee and supervisor.

- Timesheets are promptly submitted from each state liquor store for timely entry to I-Time by our Payroll Specialist. Timesheets submitted without proper signature require the employee's signature before the current SCO payroll processing cycle deadline. Supervisors will obtain the applicable employee's signature the next working day and forward that document by fax to the Payroll Department. The signed document will be stapled to the original faxed timesheet and the original will be kept on file at the store: (these timesheets are marked 'signature on file').
- Our Payroll Specialist has started an on-site training process with the state liquor stores on the use of I-Time. This program enables the personal password used by each employee to act as their signature. This training process is scheduled for completion by fiscal year end.

Sincerely yours,

  
Dyke Nally  
Superintendent

# APPENDIX

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## HISTORY

The Liquor Control Act of 1935 created State liquor stores, and a three-man Commission was given responsibility for the stores' operation. In 1939, a bill was passed which abolished the Liquor Control Commission and established the State Liquor Dispensary governed by a three-member Liquor Board. In 1941, the Idaho Liquor Board was abolished and the Office of the Superintendent was created. Reorganization placed the Liquor Dispensary in the Office of the Governor beginning July 1, 1974.

## ORGANIZATION

The superintendent is appointed by the Governor for a three-year term, and is charged with various statutory duties associated with the regulation and the control of packaged liquor products. The superintendent has organized the Dispensary into five functional areas: store operations, purchasing, accounting, information technology, and human resources.

The store operations area is primarily a service function. It is responsible for all phases of merchandising packaged liquor products to the general public. This requires establishment and operation of retail outlets that are readily accessible to the public and an efficient warehousing program to supply those outlets. The other areas in the organization are supportive functions necessary to the store operations area.

The Dispensary currently has 161 retail outlets. Of those, 59 are State stores, and 102 are contract stores.

## STATUTORY AUTHORITY

In 1934, Article III, Section 26 of the Idaho Constitution was ratified, giving the legislature authority to regulate and control intoxicating liquors for beverage purposes. The authority for the State Liquor Dispensary is found in Idaho Code, Title 23. This is the Idaho Liquor Act originally passed in 1939.

The Idaho Liquor Act, Section 23-102, states, "The public interest requires that traffic in alcoholic liquor be regulated and controlled by the State, through the medium of a state liquor dispensary vested with exclusive authority to import and sell such liquor, with certain exceptions, which are subject to its regulation."

The powers and duties of the Liquor Dispensary are provided in Idaho Code, Section 23-203, stating in part, "The Dispensary shall so exercise its powers as to curtail the intemperate use of alcoholic beverages. It shall not attempt to stimulate the normal demands of temperate consumers thereof, irrespective of the effect on the revenue derived by the state from the resale of intoxicating liquor."

The State Liquor Dispensary is funded by revenues derived from the sale of packaged alcoholic beverages and miscellaneous receipts.

The retail price of packaged alcoholic beverages is controlled by both statutory provisions and the superintendent. Idaho Code, Section 23-207(h) allows the superintendent to fix the sales price of packaged alcoholic beverages. The markup that the superintendent sets is used to offset Dispensary expenses and to benefit counties, cities, and various State agencies. Idaho Code, Section 23-217, provides that a 2% surcharge be added to the price of goods sold. The purpose of the surcharge is to provide a funding source for the Drug and Family Court Services Fund, as set forth in Idaho Code, Section 1-1625.

## STATUTORY DISTRIBUTIONS

Idaho Code requires the Dispensary to distribute cash in excess of operational needs to various State funds and Idaho cities and counties. The statutory distributions required each year are:

|                    |                             |
|--------------------|-----------------------------|
| \$1,200,000        | - Alcoholism Treatment Fund |
| 300,000            | - Community College Fund    |
| 1,200,000          | - Public School Income Fund |
| 650,000            | - Cooperative Welfare Fund  |
| <u>1,800,000</u>   | - Cities and Counties       |
| <u>\$5,150,000</u> |                             |

After the above distributions are made, 40% of the remainder is distributed to the State General Fund, and 60% is distributed to cities and counties.

The portion the cities and counties receive is further split, with 40% going to counties and 60% to cities.

The counties share is divided amongst the 44 counties based upon liquor sales within each county.

The cities share is divided amongst the 200 incorporated cities within the State, with 90% going to those cities with a liquor store or distribution station within its city limits based on liquor sales within each city. The other 10% is distributed to cities without a liquor store or distribution station based upon population.

